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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

ROBERT E. DINEEN, Superintendent of Insurance of the State of New York, as Liquidator of Lawyers Mortgage Company,
Petitioner,

v.

THE UNITED STATES OF AMERICA.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF

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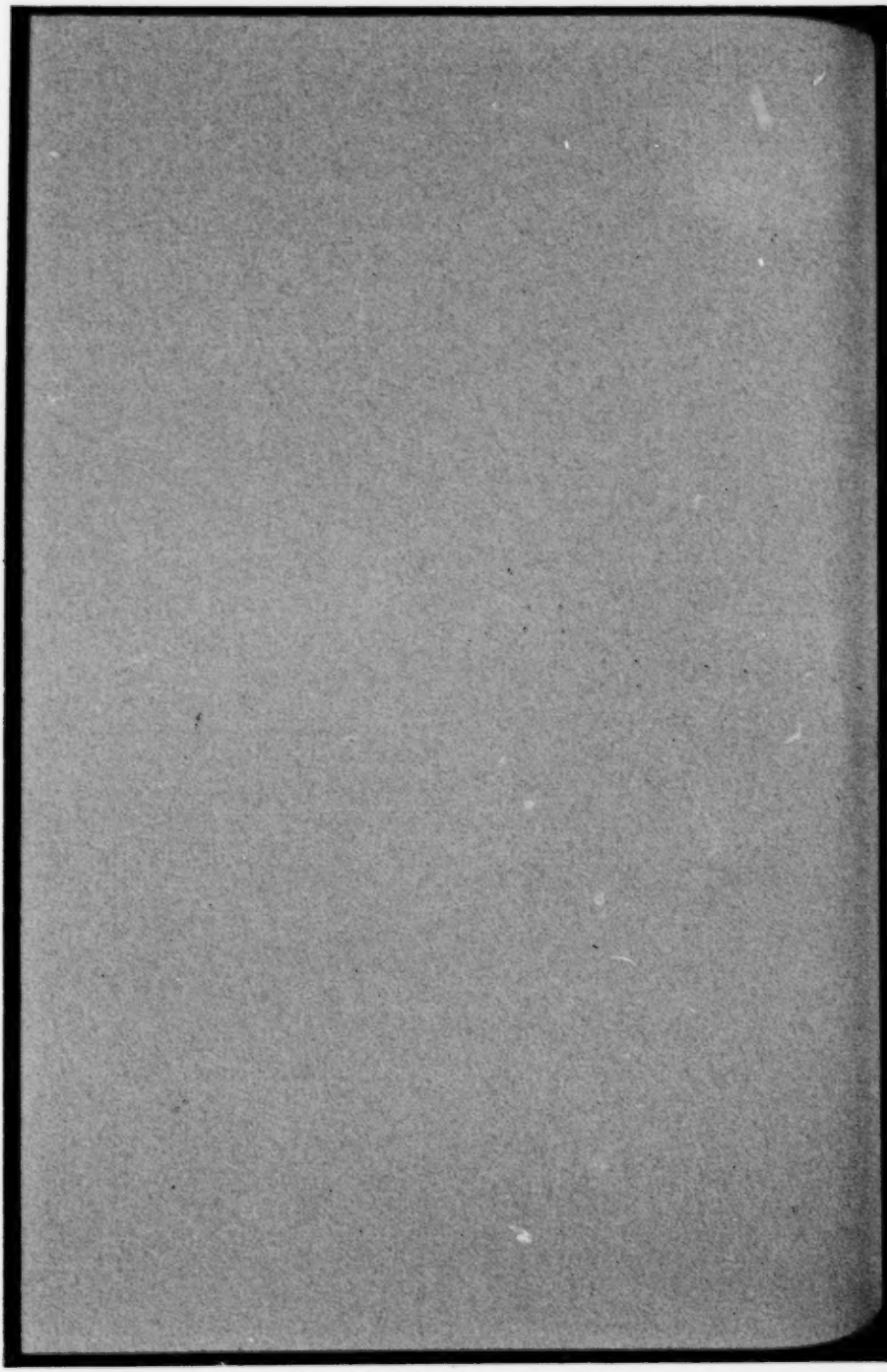

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Petition

Samuel Markowitz, counsel, on behalf of the petitioner, Robert E. Dineen, Superintendent of Insurance of the State of New York, as Liquidator of Lawyers Mortgage Company, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above entitled cause on February 6, 1946 (R. 179), affirming the judgment of the United States District Court for the Southern District of New York (R. 169-170).

Question Presented

Whether Lawyers Mortgage Company, a corporation organized under the insurance law of the State of New York, engaged in the business of making real estate mortgage loans, selling such mortgages with its policy or certificate of mortgage guarantee and receiving premiums for such guarantee, was an insurance company for the year 1931, subject to the tax imposed by Section 204 of the Revenue Act of 1928, and therefore not taxable under that Section on its income from fees and charges for services rendered in connection with the making or extending of mortgage loans.

Statute Involved

Section 204 of the Revenue Act of 1928, c. 852, 45 Stat. 791—set out in the Appendix, pp. 15-17, infra.

Statement

Lawyers Mortgage Company, hereinafter referred to as the Company, a New York insurance corporation, paid an income tax for the year 1931 as an ordinary business corporation (R. 127). Subsequently, the Company was taken over for rehabilitation by the Superintendent of Insurance of the State of New York, and he, as Rehabilitator of the Company, filed a claim for refund of part of the tax paid, on the ground that the Company was an "insurance company other than life or mutual", subject to tax under Section 204 of the Revenue Act of 1928, and, therefore, not taxable on its income from sources other than those specified in that section (Exhibit A-5, R. 131, 142). The claim for refund not having been allowed nor rejected by the Commissioner of Internal Revenue, suit for refund was thereafter brought in the United States District Court for the Southern District of New York (R. 1). The cause was

tried without a jury, upon an agreed statement of facts (Exhibit A, R. 121-130) and upon oral testimony. The District Court directed judgment for the defendant (R. 168).

The Company was organized under the insurance law of the State of New York, on or about February 9, 1893 (R. 123). Its charter was twice amended, the last time in 1913, authorizing it to do a title and mortgage guarantee business (R. 123). Since 1913 and during the year 1931, the Company carried on a mortgage guarantee business (R. 124).

The business of the Company in 1931 was selling and guaranteeing whole mortgages on New York real estate and participations in real estate mortgages (R. 29, 30), extending maturing mortgages and guarantees (R. 36, 37), and operating and selling foreclosed real estate acquired because of the Company's guarantees (R. 41, 42). The Company's procedures in the conduct of the business in 1931 were as follows:

Upon receipt of an application for a first mortgage loan on real estate, the Company would make an inspection and appraisal of the property, and, if the application was approved by the Company's loan committee, would have an examination made of the title to the real estate (R. 30). The Company would then lend the money and receive the bond and mortgage (R. 31).

The Company would at the same time make a charge to the borrower, covering the cost of the inspection and appraisal of the property, and in the case of building loans, additional inspections in the course of construction (R. 31, 32). The charge was usually 1% of the principal amount for an ordinary loan, and 3% for a building loan, and was called, on the books of the Company, a lending fee (R. 31, 32).

The Company would then sell the mortgage at its face amount and would insure to the purchaser the payment of principal and interest, for an annual charge of ½ of 1% of the principal amount, so that the purchaser of a mort-

gage bearing interest at the rate of 6% would receive an insured rate of 5½% (R. 32).

Sometimes a mortgage was too large to be assigned as a whole mortgage. In such case, the Company would issue guaranteed participation certificates in the mortgage, or in a group of mortgages (R. 33).

When a whole mortgage was sold to a single purchaser, the Company delivered to the purchaser its policy of mortgage guarantee, and when only a part of a mortgage was sold, the purchaser was given its guaranteed participation certificate (R. 33). Each policy or certificate guaranteed the payment of the principal amount thereof and of interest at an agreed rate, which was usually ½ of 1% less than the rate specified in the bond and mortgage (Exhibits E-G, R. 32). This interest differential of ½% retained by the Company was called in the policy the premium for its guarantee (Exhibit E).

Except in the case of building loans which would not be assigned until the building had been completed, the Company sold the mortgages or the participation certificates almost immediately after the loans were made (R. 74). The Company never made a profit on the sale of the mortgages or certificates; they were always sold at their face amount (R. 32).

When a mortgage was about to mature and the property owner desired an extension, the Company would make another inspection and appraisal, and upon renewal of the loan and of its guarantee, would charge the owner a fee to cover the expenses of inspection and appraisal (R. 39). This charge was never more than 1% and was called, on the books of the Company, an extension fee (R. 41).

In the event of default by the property owner, the Company would pay the guarantee holder the amount due him for principal and interest, would then foreclose the mortgage and take title to the real estate (R. 41, 42). Thereafter, the Company would operate and sell such real estate, and during the year 1931, it sustained losses of $421,771.97 on the sale of such foreclosed real estate (R. 90).

Ever since its incorporation in 1893, and during the year 1931, the Company was always subject to examination by and under the supervision of the Superintendent of Insurance of the State of New York, was always subject to the provisions of the New York insurance law applicable to title and credit guaranty corporations organized thereunder, was always subject to the regulations of the Superintendent of Insurance, and was always required to file and did file with the Superintendent of Insurance, the annual statements required by him on forms approved by him (R. 128).

The Company filed its income tax return for the calendar year 1931 with the Collector of Internal Revenue for the Third District of New York, and reported therein its gross income as follows (R. 127, 143):

Premiums	$2,051,721.67
Interest on mortgages	810,151.30
Interest on bank deposits	35,643.34
Rents	279,526.23
Profit on sale of U. S. bonds	35,499.99
Lending fees	779,302.18
Extension fees	275,498.84
Total	$4,267,343.55

Of the above total income of $4,267,343.55, the amount of $779,302.18 represents fees and charges for inspections, appraisals and other services in connection with the making of mortgage loans, and the amount of $275,498.84 represents fees and charges for such services in connection with the extending of mortgage loans.

In 1932, this Court decided the case of *Bowers* v. *Lawyers Mortgage Co.*, 285 U. S. 182, 52 S. Ct. 350, 76 L. Ed. 690, wherein it held that the Company was not taxable as an insurance company for the years 1922 and 1923 because its income from insurance for those years was less than one-third of its total income.

The amount of mortgages and mortgage certificates guaranteed by the Company outstanding at the end of the year 1922 was $149,433,293.00, and outstanding at the end of the year 1931 was $434,870,083.00 (R. 128).

The District Court held that the Company during the year 1931 was not an insurance company within the meaning of Section 204 of the Revenue Act of 1928, and directed judgment for the respondent (R. 168), 60 F. Supp. 37. Upon appeal to the Circuit Court of Appeals, the judgment was affirmed (R. 179), 153 F. (2d) 425.

Specifications of Errors to Be Urged

1) The Circuit Court of Appeals erred in holding that the "character" of the business done by the Company in 1931 is not determined by the proportionate amounts of income derived from insurance.

2) The Circuit Court of Appeals erred in holding that the Company was not an insurance company other than life or mutual for the year 1931.

Reasons for Granting the Writ

1) The issue involved in this case is important in the administration of the tax laws. Although the case arises under the provisions of the Revenue Act of 1928, which taxed insurance companies on income from specific sources only, the question whether mortgage guaranty companies are taxable as insurance companies or as ordinary business corporations is still important because under the Internal Revenue Code insurance companies are entitled to certain benefits in the computation of their income and excess-profits taxes.

2) The issue involved in this case depends on the proper interpretation of the decision of this Court in the case of

Bowers v. *Lawyers Mortgage Co.*, 285 U. S. 182, where the Court said, at page 188, that "the character of the business actually done in the tax years determines whether it was taxable as an insurance company." The Court did not define the term "the character of the business" but indicated how it should be determined. The decision of the Circuit Court of Appeals appears to be in conflict with the determination of this Court. The decision is also directly at variance with the determination of the Circuit Court of Appeals for the Third Circuit in the case of *National Commercial Title & Mortgage Guaranty Co.* v. *Duffy, et al.*, 132 F. (2d) 86.

3) The petitioner believes that the Circuit Court of Appeals failed to apply to the instant case the decision of this Court in *United States* v. *Home Title Insurance Co.*, 285 U. S. 191, 52 S. Ct. 319, 76 L. Ed. 695, decided with the *Bowers* case, supra, and that the decision of the Circuit Court of Appeals is probably in conflict with that decision of this Court. This Court found that Home Title Insurance Co. was an insurance company subject to tax as such because its income from insurance and other sources incident to insurance was the major portion of its income, while, the Circuit Court of Appeals in the instant case held that the proportion of income received from insurance activity had nothing to do with the question whether a company was subject to tax as an insurance company.

4) The Circuit Court of Appeals conceded that the petitioner found support for his contention that the Company was an insurance company in 1931, in Section 29.3797-7 of Treasury Regulations 111 but held in effect that such regulation was contrary to the decision of the *Bowers* case, supra. This Treasury regulation has been in effect since 1937 and should have been given weight in determining what "character of the business actually done" means. *Massachusetts Mutual Life Ins. Co.* v. *United States*, 288 U. S. 269, 53 S. Ct.

337, 77 L. Ed. 739; *Brewster* v. *Gage*, 280 U. S. 327, 50 S. Ct. 115, 74 L. Ed. 457; *Helvering* v. *R. J. Reynolds Tobacco Co.*, 306 U. S. 110, 59 S. Ct. 423, 83 L. Ed. 536.

For these reasons, it is respectfully submitted that the petition should be granted.

SAMUEL MARKOWITZ,
Counsel for Petitioner.

April, 1946.